

Review: 4251
Statewide Single Audit
Year Ended June 30, 2005
Illinois Student Assistance Commission

05-06. The auditors recommend ISAC review the current process for reporting financial information to the IOC and implement changes necessary to ensure the timely submission of complete and accurate forms. This process should include a reconciliation of the reporting packages to the accounting system and reports submitted to federal agencies. Additionally, ISAC should ensure a supervisory review is performed by a person knowledgeable of the reporting requirements prior to submission to the IOC. (Repeated-2002)

Findings: ISAC does not have an adequate process to ensure that financial information submitted to the Illinois Office of the Comptroller (IOC) is accurate and timely.

During the review of the financial reporting process, the auditors noted that the ISAC information for the preparation of the State's financial statements and SEFA was not completed in a timely manner. Additionally, several correcting journal entries were required to accurately state amounts reported by ISAC.

In discussing this with ISAC officials, they stated that the increasing complexity of the student loan programs coupled with the number of parties involved in the financial reporting process makes it difficult to finalize the financial information within the required timeframe.

Response: ISAC concurs and would like to note that due to the complexity of the student loan programs and the number of parties involved, the GAAP reporting process has become quite complex. The Commission made all efforts and was in constant communication with the Illinois Office of the Comptroller and the auditors prior to the end of the fiscal year to ensure that the year-end process and the processes for reporting federal expenditures was timely and accurate.

ISAC is committed to continue working with the Illinois Office of the Comptroller, the external auditors and the Illinois Office of the Auditor General to ensure timely completion of the SCO reporting requirements. To address this concern the agency is continuing to review internal processes and will consult with the Illinois Office of the Comptroller on reporting process improvements.

Updated Response: Implemented. The Commission has reviewed internal procedures and implemented changes to address the timely and accurate submission of financial statements. We do not anticipate that this finding will be repeated.

05-69. The auditors recommend ISAC consult with the USDE to interpret the federal laws and regulations relating to the processing and submission of reinsurance claims to the USDE and make necessary changes to conform with those requirements including the establishment of a post-claim review process which meets the requirements of the USDE. (Repeated-2003)

Findings: During FY03, the U.S. Department of Education Office of the Inspector General (ED-OIG) conducted an audit of the Federal Family Education Loan program to determine if, for the period October 1, 2002 through June 30, 2003, ISAC (1) adequately processed post-default collections related to administrative wage garnishments, and (2) properly submitted eligible reinsurance claims to USDE for defaulted student loans (default claims).

The final audit report received from ED-OIG indicated ISAC did not comply with the regulations regarding the submission of eligible reinsurance claims. The report stated ED-OIG reviewed 50 reinsurance claims, totaling \$123,521, selected from a universe of 21,732 reinsurance claims submitted during the audit period. Of the 50 claims tested, the report indicated 32 claims, totaling \$75,077, should have been returned to the lenders because the claim packet was missing accurate collection and/or payment histories or contained evidence of a due diligence violation(s). In addition, the ED-OIG report stated ISAC's claims review process is not adequate as it is limited to a brief review of summary information reported on the claim form submitted by the lender which does not provide adequate assurance that only claims submitted by lenders exercising required due diligence in servicing the loan were paid.

During the year ended June 30, 2005, ISAC has not changed its process for submission and payment of claims. However, subsequent to the ED-OIG audit in 2003, the USDE established an exceptional performer designation for certain lenders and lender servicers. Under this relatively new program, lenders that meet the exceptional performer requirements, including having a compliance audit of their loan portfolio which shows a performance rating of 97% or higher, receive 100% reimbursement on claims and are entitled to receive payments immediately without a claim review by ISAC. During FY05, ISAC received \$76.2 million out of a total of \$122 million reinsurance claims from lenders that were designated as exceptional performers by the USDE. Accordingly, ISAC's current potential noncompliance is mitigated by the fact that 63% of the current claims are submitted by lenders who have been designated as exceptional performers. For these lenders, ISAC must pay the claim regardless of whether they identify potential violations of the requirements relating to repayment conversion, due diligence, or timely filling.

In discussing these conditions with ISAC officials, they state the conditions identified surround a well-documented disagreement between ISAC and other guarantors across the country, and the Department of Education concerning interpretations of federal guidance and, in particular, the legitimacy of the Common Claim Initiative, which has been in place for numerous years. ISAC believes their current procedures conform with industry practice and federal regulations as interpreted in the Common Manual. In a recent letter dated December 19, 2005 from the General Manager for Financial Partner Services, Student

Financial Aid, of the USDE to the National Council of Higher Education Loan Programs (NCHELP), the USDE indicated that a post-claim review process implemented on a sample basis may form the basis for a comprehensive review which would help satisfy the claim processing requirement described above. ISAC is currently working with the ED-OIG and the USDE to resolve the findings and implement a post-claim review process.

Failure to process claims in accordance with the federal regulations could result in the payment of ineligible claims and result in unallowable costs.

Response: ISAC concurs with the recommendation calling for continued consultation with the USDE relative to the interpretation of federal laws and regulations relating to the processing and submission of reinsurance claims. As recently as January 5, 2006, ISAC appealed the preliminary determination of the USDE Federal Student Aid staff relative to the findings of the ED-OIG, for the fiscal year 2003, which gave rise to the concerns expressed in this audit. In addition, ISAC as well as ED-OIG and USDE representatives conferred on March 22, 2006 to review the audit sample, which supported the concerns outlined in the ED-OIG's audit of 2003. We expect that future consultations with the USDE including the ED-OIG will be held in an effort to satisfactorily resolve issues of concern.

ISAC has also initiated an internal project designed to establish a post-claim review process meeting the requirements of USDE as outlined in letter of December 19, 2005. It is expected that the first round of the post-claim review process, developed by ISAC, will be initiated for claims submitted during the second quarter of calendar year 2006. ISAC is also part of the student loan industry-wide work group presently formulating agreed approaches to the post-claim review process, as requested by the USDE.

Updated Response: Partially Implemented. The Commission has implemented a post-claim review process which meets, if not exceeds, the requirements outlined by the U.S. Department of Education (USDE) in their letter of December 19, 2005. This process has been in place since the second quarter of calendar year 2006. ISAC is also part of the student loan industry-wide work group which has submitted agreed proposals to the USDE to implement a standard post-claim review process.

The Commission has an appeal pending with the USDE challenging the accuracy of the data on which this finding is based. Based on the outcome of this appeal and any subsequent discussions, ISAC will modify our claims process, as appropriate.

05-70. The auditors recommend ISAC implement changes to the loan information system (Odyssey) configuration to ensure notification letters are sent to defaulted borrows on a timely basis.

Findings: ISAC did not inform borrowers on a timely basis of their rights and obligations for defaulted loans.

During testwork of 30 borrowers who entered into default, the auditors noted seven instances where the notification letter was not generated by the loan information system.

Upon further discussion with management, we were informed that ISAC had identified system configuration problems including notification letters for borrowers with multiple loans. In these situations, the loan information system would generate a notification for the first loan of a borrower that defaulted, but would not generate additional letters for subsequent loans that went into default. ISAC officials identified the problem and implemented manual procedures starting in August 2005 to identify all borrowers that required notification letters to be sent. During the year ended June 30, 2005, there were approximately 3,800 defaulted loans for which a notification letter was not generated by the loan information system and were not sent within the required 30 days.

Response: ISAC concurs and implemented procedures in August of 2005 designed to create a manual means of generating required letters to this subset of borrowers in default. A request to make the programmatic changes to systematically generate the required letters is presently in the work queue. Until such time as the programmatic changes are made, ISAC will continue with the manual means of generating the required letters.

Updated Response: Implemented. The Commission implemented procedures in August of 2005 to create a manual means of generating required letters to this subset of borrowers in default. We do not anticipate that this finding will be repeated.

05-71. The auditors recommend ISAC establish procedures to ensure borrower payments from outside collection agencies are received on a timely basis.

Findings: ISAC receives payments on defaulted loans directly from borrowers and indirectly through outside collection agencies. Borrower payments received by outside collections are generally remitted to ISAC bi-weekly which extends the period between receipt of the borrower payments (received from outside collection agencies) and deposited into the federal fund. During testwork of 30 borrower payments, the auditors noted 8 instances where borrower payments were not deposited into the federal fund within the required 48 hours. The delays ranged between 4 and 99 days.

In discussing these conditions with ISAC officials, they stated that delays in receipt of borrower payments from outside legal collection agencies were the reason for non-compliance with the 48-hour rule.

Response: ISAC has thoroughly evaluated its deposit process and is working with the outside legal collection agencies to reduce processing time for depositing collections into the Federal Fund. In addition, ISAC continues to transfer interest on a monthly basis for those deposits that fall outside the 48-hour deposit period into the Federal Fund.

Updated Response: Accepted. ISAC continues to work with the outside legal collection agencies to reduce processing time for depositing collections into the Federal Fund.

05-72. The auditors recommend ISAC assign all defaulted loans to the USDE that meet the criteria contained in federal regulations or obtain a written waiver which specifies the number and criteria for assignment of loans to the USDE. (Repeated-2004)

Findings: ISAC is required to assign all defaulted loans that meet certain criteria as of April 15th of each year to the USDE. During the audit of the Federal Family Education Loan Program, the auditors noted there were approximately 9,009 defaulted loans that meet this criteria as of April 22, 2005 that should have been assigned to the USDE but were not. Management indicated it was their practice to only assign approximately 10,000 loans per year.

In discussing these conditions with ISAC officials, they state that while offering no dispute relative to the interpretation of the regulation in question, the Department of Education has consistently indicated their satisfaction with ISAC's process of subrogating loans. Further, understandable time, effort and personnel limitations have prevented the immediate subrogation of all loans which might be eligible for such treatment.

Response: ISAC concurs and is presently seeking to assign all defaulted loans to the USDE meeting the criteria stated in the relevant federal citation.

On the matter of a written waiver, ISAC provided a letter to the USDE on May 31, 2005 identifying an assignment schedule which would result in the assignment of nearly 17,000 loans over a two year period (beginning in October 1, 2003 and continuing through September 30, 2005). While the letter to the USDE has never been addressed by Department officials, the schedule outlined in that letter is serving as the basis for current assignment activity.

Updated Response: Accepted/Partially Implemented. The Commission continues to actively assign loans, eligible for assignment to the USDE. This process has resulted in significant progress in ensuring that all loans, eligible for assignment, receive such treatment in a timely fashion.

05-73. The auditors recommend that ISAC follow the written policies and procedures requiring the completeness and accuracy of imaging be verified before claims packets are destroyed and establish controls to ensure policies and procedures are followed. (Repeated-2003)

Findings: ISAC does not have an adequate process to ensure that original documentation submitted by lenders for reinsurance claims are accurately and completely imaged for document retention requirements of the Federal Family Education Loan Program.

In discussing these conditions with ISAC officials, they stated a combination of factors contributed to the condition including issues with the print range of a specific servicer's documents being incompatible with the scanning equipment and the ability of the imaging software to register the date stamp on a document.

Response: ISAC concurs and notes that the agency has written procedures requiring the completeness and accuracy of imaged claim files and, in addition to the quality assurance steps itemized below, will be following quality assurance post-claim sampling as part of the Common Manual approach and approved by the USDE.

- As of February 15, 2005, Data Management staff perform quality control and review the claim files after they are scanned and indexed. This was implemented to address the issue of missing imaged information due to the incompatible print range of the documents. The original source documents are retained if information is missing on the imaged copy of the claim file. To date, ISAC is retaining approximately 3,000 original files due to incompatible print range of the source documents.
- A second level of review was implemented on May 5, 2005, which requires Data Management staff to quality control and review date stamps on claim forms to ensure legibility. The original source documents are retained if the date stamp is illegible. Since this QA review was implemented, 1,934 original files have been retained due to illegible date stamps. To further alleviate this issue, new date stamps were purchased by ISAC in March 2006 after thorough and successful testing to ensure date stamp legibility.

Updated Response: Implemented. The Commission has documented operating policies and procedures for imaging, provided additional staff training and has established an internal reconciliation process. We do not anticipate that this finding will be repeated.